

# FDIC State Profile

Spring 2005

## Tennessee

The outlook remains positive for labor markets in Tennessee.

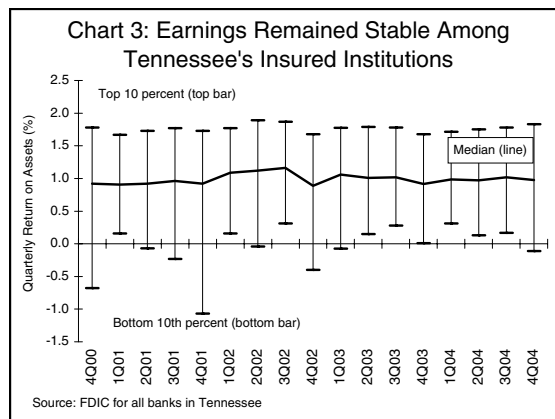
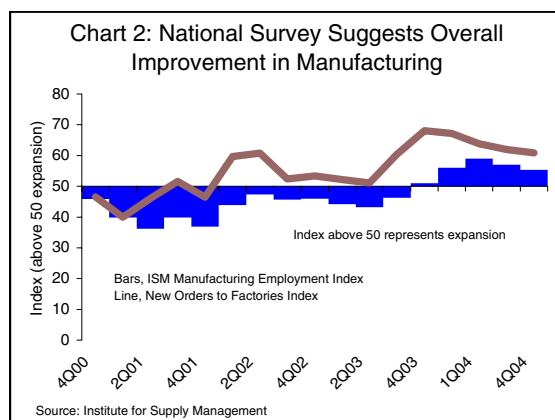
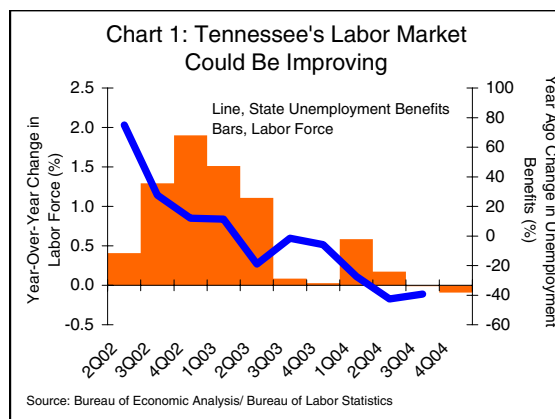
- Employment levels in Tennessee grew 1.5 percent in fourth quarter 2004, the fifth consecutive quarterly improvement.
- Employment growth was strongest in the business services, construction, education and health, and leisure and hospitality sectors, while job losses occurred in telecommunications, and state and local government.
- Claims for unemployment insurance benefits continue to decline, a generally accepted sign that near-term job market conditions will remain positive (See Chart 1).
- The improvement was widespread with 82 out of 95 counties reporting a decline in the jobless rate. The lower unemployment rates were particularly impressive considering the fact that more workers entered the labor force during the period.

### Growth in manufacturing continues.

- Job growth in Tennessee's manufacturing sector grew 0.3 percent on a year-over-year basis in fourth quarter 2004, the second consecutive quarterly gain in more than three years. Employment growth was strongest in the auto-related businesses, including transportation equipment and motor vehicle parts.
- Economists at Tennessee State University attribute growth in the auto-related sectors to recent expansions by Nissan in **Smyrna** and **Decherd**, Peterbilt Motors in **Madison**, and General Motors Corporation in **Spring Hill**.
- The near term prospects for the manufacturing segments appear bright with two leading Institute for Supply Management indices suggesting positive improvements in the months ahead (See Chart 2).

### Residential real estate markets set records in 2004, while commercial markets began to improve.

- **Memphis** and **Nashville** metropolitan home sales set records in 2004 and contributed to strong employment growth in the construction industry. Memphis home sales



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surged 13.8 percent from the previous year, while sales in Nashville rose nearly 14 percent.

- The National Association of Realtors predicts that after four consecutive record years, home sales should ease but remain close to record levels. Despite generally favorable signs, incentives offered by builders in the Memphis market have become more common at certain price points, suggesting some softening may already be occurring.
- The continued strength in this sector of the economy will be heavily influenced by interest rates. Given the uncertainty of interest rate movements, lenders will be well served to closely monitor local housing trends and be prepared to initiate appropriate measures to mitigate risk if conditions deteriorate unexpectedly.
- Memphis and Nashville office and industrial markets ended 2004 with some positive absorption. Prospects for further improvement in 2005 appear to be good since the economic outlook is widely regarded as positive and limited new space is expected to be delivered in both markets. Despite the generally positive trends, some challenges remain, including expiration of office leases originated during a period of higher rates and prospects of rising costs, such as property, insurance, and utilities.

### Return on assets (ROA) remained steady at year-end 2004.

- Median ROA among insured institutions in Tennessee was 0.98 percent at year-end 2004, down slightly from 1.02 percent in third quarter 2004 and on par with one year ago (See Chart 3). More than half of the insured institutions in the state's rural areas experienced an increase in ROA, which offset a decline in ROA by nearly 60 percent of all insured institutions in the state's metropolitan areas.

### The use of noncore funding sources<sup>1</sup> peaked among banks in Tennessee.

- Growth in traditional funding sources has stagnated at many banks in recent years and largely has failed to keep up with the growth in bank assets, particularly loans. In fact, loan growth significantly exceeded core deposit growth for the 12 months ending December 31, 2004.
- In response to strong loan demand, state institutions have had to supplement traditional funding sources with a variety of new, noncore funding instruments. This change is evidenced by a peak in median noncore funding to total assets among insured institutions in Tennessee at year-end

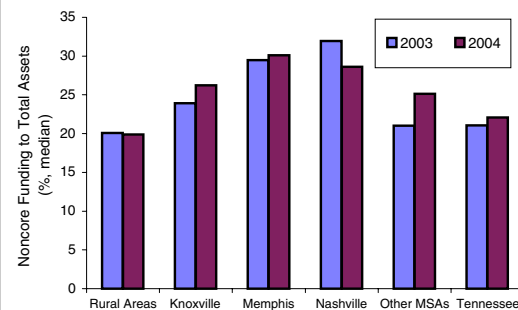
2004. The increasing reliance on noncore funding sources has been more pronounced in the state's major metropolitan markets (See Chart 4).

- A greater reliance on noncore funding, combined with the competitive nature of these markets, may exacerbate funding costs and pressure net interest margins among insured institutions in a rising rate environment.

### Metro Spotlight: Nashville's loan levels reached record high in 2004.

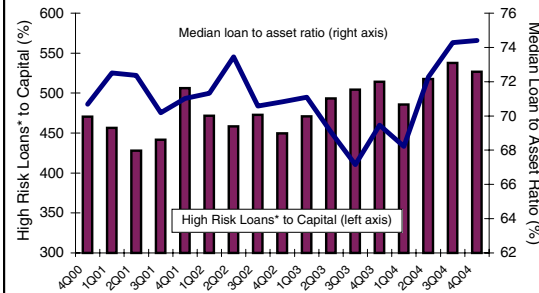
- Loans made by established insured institutions<sup>2</sup> in Nashville peaked at \$5.3 billion at year-end 2004, up 36 percent from one year ago. As a result, the median loan to asset ratio also reached an all time high of 74.4 percent at year-end 2004.
- Increased loan demand was driven in large part by growth in the generally higher yielding loans secured by real estate and by growth in commercial and industrial loans. These combined loans represented a median figure of nearly 530 percent of capital in fourth quarter 2004, slightly below the previous peak of 538 percent one quarter ago (See Chart 5).

Chart 4: Noncore Funding Remains High in Tennessee's Major Metro Markets



Source: FDIC, excludes banks established within the past three years

Chart 5: Loan Levels Peaked in 2004 Among Insured Institutions in Nashville



\*High risk loans are defined as construction and land development secured by real estate; loans secured by multifamily residential properties; loans secured by nonfarm, nonresidential properties; and commercial and industrial loans. Source: FDIC for established banks in Nashville

<sup>1</sup>Noncore funding sources include brokered deposits, certificates of deposits in the amount of \$100,000 or more, federal funds purchased and securities sold subject to repurchase agreements, and other borrowed funds.

<sup>2</sup>Established insured institutions are defined as those in existence for three years or more.

## Tennessee at a Glance

**ECONOMIC INDICATORS** (Change from year ago quarter, unless noted)

<b>Employment Growth Rates</b>	<b>Q4-04</b>	<b>Q4-03</b>	<b>Q4-02</b>	<b>Q4-01</b>	<b>Q4-01</b>
Total Nonfarm (share of trailing four quarter employment in parentheses)	1.5%	0.1%	0.4%	-2.6%	0.7%
Manufacturing (15%)	0.3%	-2.9%	-3.1%	-8.5%	-3.5%
Other (non-manufacturing) Goods-Producing (5%)	1.8%	0.6%	-2.8%	-4.1%	-0.9%
Private Service-Producing (65%)	2.1%	0.8%	1.3%	-1.8%	1.8%
Government (15%)	0.3%	-0.3%	1.5%	1.7%	1.7%
Unemployment Rate (% of labor force)	5.3	5.6	5.3	4.9	4.1

<b>Other Indicators</b>	<b>Q4-04</b>	<b>Q4-03</b>	<b>Q4-02</b>	<b>Q4-01</b>	<b>Q4-01</b>
Personal Income	N/A	6.1%	3.2%	3.3%	4.8%
Single-Family Home Permits	7.5%	17.8%	14.3%	10.2%	-25.0%
Multifamily Building Permits	-26.8%	82.0%	115.2%	-76.3%	-11.4%
Existing Home Sales	14.2%	16.4%	20.3%	4.1%	-1.3%
Home Price Index	4.5%	3.6%	3.2%	5.1%	3.5%
Bankruptcy Filings per 1000 people (quarterly level)	2.36	2.61	2.75	2.70	2.22

**BANKING TRENDS**

<b>General Information</b>	<b>Q4-04</b>	<b>Q4-03</b>	<b>Q4-02</b>	<b>Q4-01</b>	<b>Q4-01</b>
Institutions (#)	208	208	213	213	221
Total Assets (in millions)	133,491	118,572	115,452	105,935	91,998
New Institutions (# < 3 years)	14	13	17	23	21
Subchapter S Institutions	39	38	32	31	24

<b>Asset Quality</b>	<b>Q4-04</b>	<b>Q4-03</b>	<b>Q4-02</b>	<b>Q4-01</b>	<b>Q4-01</b>
Past-Due and Nonaccrual Loans / Total Loans (median %)	1.75	2.43	2.57	3.02	2.68
ALLL/Total Loans (median %)	1.31	1.35	1.34	1.29	1.26
ALLL/Noncurrent Loans (median multiple)	2.33	1.80	1.70	1.52	1.85
Net Loan Losses / Total Loans (median %)	0.16	0.26	0.29	0.32	0.19

<b>Capital / Earnings</b>	<b>Q4-04</b>	<b>Q4-03</b>	<b>Q4-02</b>	<b>Q4-01</b>	<b>Q4-01</b>
Tier 1 Leverage (median %)	9.67	9.38	9.35	9.21	9.39
Return on Assets (median %)	0.96	0.98	1.06	0.89	1.01
Pretax Return on Assets (median %)	1.37	1.39	1.46	1.25	1.40
Net Interest Margin (median %)	4.22	4.19	4.30	4.10	4.32
Yield on Earning Assets (median %)	5.83	6.05	6.81	8.08	8.64
Cost of Funding Earning Assets (median %)	1.55	1.83	2.48	4.04	4.33
Provisions to Avg. Assets (median %)	0.18	0.23	0.31	0.31	0.22
Noninterest Income to Avg. Assets (median %)	0.80	0.79	0.77	0.78	0.72
Overhead to Avg. Assets (median %)	3.17	3.16	3.11	3.03	3.00

<b>Liquidity / Sensitivity</b>	<b>Q4-04</b>	<b>Q4-03</b>	<b>Q4-02</b>	<b>Q4-01</b>	<b>Q4-01</b>
Loans to Assets (median %)	67.7	66.8	65.9	65.6	67.3
Noncore Funding to Assets (median %)	22.1	21.0	21.2	20.6	19.7
Long-term Assets to Assets (median %, call filers)	13.6	15.3	12.4	12.3	12.9
Brokered Deposits (number of institutions)	55	46	35	31	19
Brokered Deposits to Assets (median % for those above)	2.8	2.2	3.4	2.9	2.3

<b>Loan Concentrations (median % of Tier 1 Capital)</b>	<b>Q4-04</b>	<b>Q4-03</b>	<b>Q4-02</b>	<b>Q4-01</b>	<b>Q4-01</b>
Commercial and Industrial	69.2	78.1	74.3	82.2	81.3
Commercial Real Estate	213.7	192.7	184.2	164.0	156.3
Construction & Development	51.1	44.0	40.5	40.8	35.0
Multifamily Residential Real Estate	5.5	4.0	4.1	3.2	2.6
Nonresidential Real Estate	128.8	131.7	119.6	103.1	90.2
Residential Real Estate	224.5	227.4	230.3	234.2	247.9
Consumer	62.0	69.3	75.0	86.7	94.8
Agriculture	20.1	18.3	19.2	19.8	18.3

**BANKING PROFILE**

<b>Largest Deposit Markets</b>	<b>Institutions in Market</b>	<b>Deposits (\$ millions)</b>	<b>Asset Distribution</b>	<b>Institutions</b>
Memphis, TN-MS-AR	54	25,949	< \$250 mil.	152 (73.1%)
Nashville-Davidson--Murfreesboro, TN	53	23,141	\$250 mil. to \$1 bil.	48 (23.1%)
Knoxville, TN	28	8,693	\$1 bil. to \$10 bil.	5 (2.4%)
Chattanooga, TN-GA	27	6,310	> \$10 bil.	3 (1.4%)
Kingsport-Bristol-Bristol, TN-VA	26	3,675		